

Insider Trading Originating Abroad and “Waiver-by-Conduct”

I. Introduction

On July 30, 1984, the Securities and Exchange Commission solicited comments on its proposal of “waiver-by-conduct” doctrine.¹ The proposal is intended to facilitate the extraterritorial enforcement of the antifraud provisions of United States securities legislation. Under the SEC proposal, individuals would be deemed to have waived their right to the protection of foreign bank secrecy laws by purchasing or selling securities on United States markets through the auspices of foreign banks. Currently, individuals engaged in fraudulent transactions on United States markets sometimes purchase securities through the auspices of foreign banks in order to preserve anonymity. The SEC proposal seeks to deny such individuals the anonymity which foreign bank secrecy laws provide.

The waiver-by-conduct proposal cannot advance the extraterritorial enforcement of U.S. securities legislation without the cooperation of foreign governments. For two important reasons, foreign governments cannot be expected to cooperate with the waiver-by-conduct doctrine. First, the enforcement jurisdiction of the United States is not readily recognized abroad.

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1. Securities and Exchange Commission, Release No. 21186 of July 30, 1984 [hereinafter cited as Release]. See Fedders, *Policing Internationalized U.S. Capital Markets: Methods to Obtain Evidence Abroad*, 18 INT'L LAW. 89 (1984).

Second, implied waivers, such as the waiver-by-conduct doctrine, are not generally recognized as exceptions under foreign bank secrecy laws.

In 1981, the Section of International Law and Practice proposed and the American Bar Association's (ABA) House of Delegates adopted a recommendation concerning conflicts of law and policy created by the attempts of federal agencies to apply United States law overseas.² It provides that no independent federal regulatory agency should take any administrative action involving important potential conflicts of law and policy between the United States and foreign nations without prior notice to and consultations with the State Department and, whenever appropriate, the government of the affected foreign country.

The ABA's 1981 recommendation applies to the SEC's current proposal. The waiver-by-conduct doctrine involves an important potential conflict between the United States' interest in policing the integrity of its securities markets and the interest of foreign countries in preserving the inviolability of their banking systems. If the SEC were to follow ABA Recommendation No. 101A, then the SEC would reject the current proposal in favor of other more diplomatic approaches to the prosecution of securities fraud originating abroad. These approaches include treaties for cooperation in the prosecution of criminal matters, coordination of legislation and administrative cooperation. Such approaches, of course, do not ensure the effective extraterritorial enforcement of U.S. securities laws in all cases, but they do serve to avoid the needless deterioration of foreign relations where such enforcement is impossible without local cooperation.

2. BE IT RESOLVED, That the American Bar Association recommends to the President and the Congress:

A. The implementation of a United States government policy, by executive action or by legislation if necessary, providing:

1. That any independent federal regulatory agency or executive agency ("Agency") shall take a law enforcement or regulatory action of a type determined by the President to involve important potential conflicts of law and policy between the United States and foreign nations,
 - (a) as to non-national individuals or enterprises (including foreign subsidiaries of U.S. parent enterprises) located outside of the United States, or
 - (b) involving the issuance of subpoenas or investigative requests for service outside, or seeking information located outside of the United States,
 only after prior notification to, and the opportunity for consultation during a period of two calendar weeks from the date of notification with, the United States Department of State or such other executive agency as the President shall designate;

...

3. That when, on the basis of such consultations, the President determines it to be appropriate, affected foreign governments will be provided an opportunity to consult with United States government officials during the period of two calendar weeks from the date of notification to the United States State Department or such other executive agency as the President shall designate, to provide that the views of such governments may be taken into account before the law enforcement or regulatory action is taken while, at the same time, leaving the Agency free to proceed with its enforcement responsibility without undue delay.

American Bar Association Recommendation (Report No. 101) of August 12, 1981.

II. Current Situation

The SEC is charged with protecting the integrity of the securities markets located within the United States.³ The legislative mandate of the SEC applies to transactions originating abroad.⁴ However, when the efforts of the SEC propel it abroad in search of information, foreign countries can and sometimes do take issue with such efforts.

The SEC's efforts to apply U.S. securities laws to transactions originating abroad are sometimes frustrated in particular by the existence of foreign bank secrecy laws. When a bank subject to a bank secrecy law executes a transaction on behalf of a customer but in its own name, then the bank typically is precluded from disclosing any information about the transaction, including the identity of the customer. Foreign banks, subject to both the demands of the SEC to produce evidence and the demands of their local authorities to respect their customers' rights to secrecy, usually comply with the demands of their local legislation and refuse to accommodate the SEC.

When confronted with the refusal of a foreign bank to provide information, the SEC has typically resorted to two techniques: (1) the power of subpoena under Federal Rule of Civil Procedure 37 (FRCP 37) to compel production of evidence and (2) treaties for cooperation in the prosecution of criminal matters, such as the Swiss-American Treaty on Mutual Assistance in Criminal Matters [hereinafter] Treaty,⁵ to obtain the assistance of the foreign authorities in procuring evidence. Each technique has provided some success, but the SEC claims that each has its shortcomings. FRCP 37 is often rejected abroad and invariably generates hostility.⁶ The application of treaties entails substantial delays, which can diminish the value of the information obtained.⁷

III. The Proposal of the SEC

The SEC has proposed the waiver-by-conduct doctrine to overcome the difficulties created by foreign bank secrecy laws. The waiver-by-conduct doctrine provides that the purchase or sale of securities on U.S. markets constitutes consent to the disclosure of bank secrets related to that purchase or sale:

the act of effecting a purchase or sale of securities within the U.S., whether directly or indirectly, shall constitute an irrevocable consent to the disclosure of relevant evidence in connection with any investigation, court action or administrative proceeding that might arise out of the transaction.⁸

3. Securities Act of 1933 § 2(7), codified at 15 U.S.C. § 77b(7) (1983)), provides: The Term "interstate commerce" means trade or commerce in securities or any transportation or communication relating thereto . . . between any foreign country and any State, Territory, or the District of Columbia, or within the District of Columbia.

4. *Id.*

5. 27 U.S.T. 2021

6. Release, *supra* note 1, at 16.

7. *Id.* at 19.

8. *Id.* at 28-29.

The primary purpose of the SEC's proposal is to create an exception to foreign bank secrecy laws by which a customer would waive his right to secrecy when he purchases or sells securities on U.S. markets.⁹ In adopting this approach, the SEC hopes to secure the cooperation of foreign banks in obtaining information and the assistance of their governments. The banks' customers, the SEC reasons, would no longer have a basis to object to the disclosure of information because they had constructively waived their right to secrecy by placing an order on a U.S. securities market.

IV. Reactions from Abroad to Other Extraterritorial Applications of U.S. Law

Discussions of the extraterritorial application of United States laws often revolve around the justification, under principles of law accepted in the United States, for the United States to extend its jurisdictional reach beyond its shores.¹⁰ Recent experience shows, however, that the relevant issue is not the legitimacy of extending U.S. laws abroad under U.S. principles, but the legitimacy under principles of law generally accepted abroad, for rejecting the extraterritorial reach of United States law.

Recent experience also indicates that United States law cannot be effectively applied overseas against non-U.S. persons without the cooperation of foreign governments. The antitrust experience is well known and will not be discussed here.¹¹ It is sufficient to note that the application of U.S. antitrust law abroad has led to the adoption of notorious "blocking statutes" by even

9. *Id.* at 21.

10. See e.g., *SEC v. Banca Della Svizzera Italiana*, 92 F.R.D. 111 (S.D.N.Y. 1981). THE RESTATEMENT (SECOND) OF FOREIGN RELATIONS LAW § 40 (1965) (hereinafter cited as RESTATEMENT) sets out a balancing test for resolving conflicts created by the coextensive application of regulations dictating inconsistent conduct:

Limitations on Exercise of Enforcement Jurisdiction

Where two states have jurisdiction to prescribe and enforce rules of law and the rules they may prescribe require inconsistent conduct upon the part of a person, each state is required by international law to consider, in good faith, moderating the exercise of its enforcement jurisdiction, in the light of such factors as

- (a) vital national interests of each of the states,
- (b) the extent and the nature of the hardship that inconsistent enforcement actions would impose upon the person,
- (c) the extent to which the required conduct is to take place in the territory of the other state,
- (d) the nationality of the persons, and
- (e) the extent to which enforcement by action of either state can reasonably be expected to achieve compliance with the rule prescribed by that state.

See also Dam, *Economic and Political Aspects of Extraterritoriality*, 19 INT'L LAW. (1985), and *Symposium: The Revised Restatement*, 19 INT'L LAW. 431-503 (1985).

11. See e.g., A. H. HERMANN, *CONFLICTS OF NATIONAL LAWS WITH INTERNATIONAL BUSINESS ACTIVITY: ISSUES OF EXTRATERRITORIALITY* 59-60. (1982).

our closest allies.¹² United States laws other than antitrust law have been applied abroad. In particular, recent experiences in export controls are instructive in identifying the probable objections to the waiver-by-conduct doctrine.

EXPORT CONTROLS

On June 22, 1982, the Department of Commerce extended the scope of the Export Administration Act to cover oil and gas equipment manufactured abroad by foreign companies under licenses from U.S. corporations.¹³ The purpose of the amendment was to prevent European companies from supplying equipment for the construction of the Siberian pipeline.¹⁴ In the end the equipment was supplied.¹⁵

The visceral reactions of some European governments to those amendments were well publicized.¹⁶ Less well publicized were the more reasoned responses to the amendment of the Export Administration Act. In particular, the Commission of the European Economic Community (hereinafter Commission) issued a position paper (hereinafter Comments) denouncing the amendments as illegal under international law and inconsistent with principles of comity, even as they are applied in the United States.¹⁷ Since the legal staff of the Commission is composed of jurists from several European countries, the Comments can be read as a European consensus on the problems created by the extraterritorial application of U.S. law. The principles set forth in the Comments can be applied to the SEC's current proposal.

First, the Commission adopted a concept of the "territoriality" principle which emphasizes the limits on the application of one nation's laws within the territory of another nation: "each state . . . has the right fully to organize and develop its social and economic system."¹⁸ In applying this principle,

12. Such statutes include: in France, Law No. 81-550 of May 12, 1981; in the United Kingdom, The Protection of Trading Interests Act—1980; in Australia, Foreign Proceedings (Prohibition of Certain Evidence) Act of 1976; in Canada, Business Records Protection Act of 1974; in West Germany, Decree No. 711 of 14 December 1966, on the Transmission or Shipping of Documents to Foreign Authorities; and in Switzerland, Swiss Penal Code, Arts. 271-274.

13. Export Administration Regulations, 15 C.F.R. § 376 as amended 47 Fed. Reg. 27251 (1982). See also Unclassified State Dept. Telex 174622 1/5 (June 24, 1982).

14. The N.Y. Times, June 24, 1982, at 1, col. 5. See also 47 Fed. Reg. 27251.

15. Int'l Her. Trib., August 27, 1982, at 1, col. 1.

16. E.g., Int'l Her. Trib., October 18, 1982, at 2, col. 1 (reporting the "expression of due concern" of the foreign ministers of the 10 Member States of the European Economic Community on the occasion of an informal two-day meeting at Nyborg, Denmark). See also Dam, *supra* note 10.

17. Comments of the European Community on the Amendments of June 22, 1982 to the U.S. Export Administration Regulations (August 10, 1982)(unpublished offset manuscript issued by the legal staff of the Commission of the European Economic Community) [hereinafter cited as Comments].

18. *Id.* at Item II.5.

which emphasizes the sovereignty of each country to set national policy, to the extension of U.S. export laws to cover equipment manufactured in Europe, the Commission found that:

The public order ("ordre public") of the European Community and its Member States is thus purportedly replaced by U.S. public policy which European companies are forced to carry out within the E.C., This is an unacceptable interference in the affairs of the European Community.¹⁹

By focusing on the right to set public policy, rather than the importance of a specific public policy, the Commission adopts a categorical approach to territoriality which differs from the interest analysis common in the United States.²⁰ The significance of this attitude for the SEC's proposal is clear. Even if the waiver-by-conduct doctrine is supported by important policy considerations and even if those policy considerations outweigh the public policy embodied in foreign bank secrecy laws, the extraterritorial extension of U.S. law would be viewed as an unacceptable intrusion into the internal affairs of other countries.

Second, the SEC's proposal requires that U.S. broker-dealers include a provision in their contracts with foreign banks giving foreign banks and their customers notice of the waiver-by-conduct law.²¹ The Comments speak directly to contractual provisions such as the one proposed by the SEC. In its Comments, the Commission rejects attempts to obtain voluntary compliance with national legislation through contractual provisions:

It is reprehensible that present U.S. Regulations encourage non-U.S. companies to submit "voluntarily" to this kind of mobilization for U.S. purposes. . . . If a Government in law and in fact systematically encourages the inclusion of such submission clauses in private contracts, the freedom of contract is misused in order to circumvent the limits imposed on national jurisdiction by international law.²²

Accordingly, foreign banks may well object to the notice of the waiver-by-conduct law inserted into contracts and feel justified in ignoring it.

Third, the Commission asserts in its Comments that the June 22, 1982 extension of U.S. export controls violates notions of comity, even under U.S. law:

If a foreign government were to take measures like the June 22 Amendments, it is doubtful whether they would be in conformity with U.S. law and they would therefore probably not be recognized and enforced in U.S. courts.²³

And again:

In the same way as the U.S. could not accept that its companies were turned into instruments of the foreign policy of other nations, the E.C. cannot accept that its

19. *Id.* at Item II. 10

20. *See* RESTATEMENT, *supra* note 10.

21. Release, *supra* note 1, at 31.

22. Comments, *supra* note 17, at Item II. 11.

23. *Id.* at Item III. 15.

companies must follow another trade policy than its own within its own territorial jurisdiction.²⁴

To support its assertion, the Commission cited Section 8 of the Export Administration Act (the foreign anti-boycott provisions),²⁵ which was enacted by the U.S. Congress to prevent U.S. corporations from complying with boycott laws enacted by Arab nations.

The foreign response to the June 22, 1982 extension of the Export Administration Act indicates that the extraterritorial application of U.S. laws evokes not only strong emotional responses, but also reasoned objections, which justify the refusal of foreign governments to cooperate in the attempts to apply United States law abroad.

V. Probable Rejection Abroad of the SEC Proposal²⁶

The SEC acknowledges that "the existence of a valid consent would be governed by foreign law."²⁷ A review of the law of most foreign countries indicates that the extent of a customer's waiver of bank secrecy protection is limited in general to the clear intention of the customer.²⁸ Since bank

24. *Id.* at Item III. 16.

25. 50 U.S.C.A. § 2407 (1982).

26. In the wake of the Release, reactions to the waiver-by-conduct proposal were published in other articles. These articles include: *Verdict on the SEC's "waiver-by-conduct" concept*, INT'L FIN. L. REV., Nov. 1984, at 4 (lawyers from seven jurisdictions, including the United States, give their own reaction to the SEC's "waiver-by-conduct" concept release); Fedders & Mann, *The "waiver-by-conduct" concept—a reply*, INT'L FIN. L. REV., Dec. 1984, at 10; "Waiver-By-Conduct": Another View, 6 J. OF COMP. BUS. AND CAP. MKT. L., 307-318 (1984) (containing the responses of six jurists and others from the United States and abroad). The competent SEC officials launched the debate concerning the waiver-by-conduct doctrine in a series of articles, the best documented of which are: Fedders, *supra* note 1; and Fedders, Wade, & Mann, *Waiver-by-Conduct—A Possible Response to the Internationalization of the Securities Markets*, 6 J. OF COMP. BUS. AND CAP. MKT. L. 1-54 (1984). In response to the request for comments contained in the Release, the SEC received sixty-five responses, the results of which are summarized in DAILY REPORT FOR EXECUTIVES (BNA) No. 32 at A-1—A-4 (February 15, 1985) ("Regulatory and Legal Developments").

27. Release, *supra* note 1, at 30. The SEC also states in the Release that a foreign bank could find itself threatened with contempt proceedings in the U.S. if "a foreign jurisdiction . . . rule[d] that the purported consent [by the customer] had no effect on its secrecy laws." (Release, *supra* note 1, at 48.) In other words, the Proposal cannot have its intended effect unless it is accepted abroad and recognized under foreign law.

28. The Release only provides brief discussions of the bank secrecy laws of Switzerland and the Bahamas. An independent review of the sources cited by the SEC suggests that the conclusions drawn in the Release are not supported by them. For example, the Release quotes Swiss bank secrecy law selected from the text of Professor Schultz, a leading commentator on Swiss banking law: "[a] client can give a bank oral or written permission to disclose a fact subject to secrecy; even tacit consent to the disclosure of the secret by implied action is sufficient" (Release, *supra* note 1 at 32). Despite the assertion of the SEC, this quote does not establish that the waiver-by-conduct proposal would be recognized in Switzerland. Other quotations from Professor Schultz's text suggest that placing an order for the purchase or sale of

secrecy exists for the benefit of the customer, a bank relies upon a waiver at its own peril. Accordingly, the banks customarily require express or even written consent. Conduct is relied upon only if it unambiguously indicates the customer's intention. Since the doctrine of waiver-by-conduct relies entirely on the principle of constructive consent imputed by law (which most probably is contrary to the intentions of the customer in the relevant cases), there would, in most instances, be no basis in foreign bank secrecy law for recognition of the SEC's proposal.²⁹

A. SWITZERLAND

The Swiss Banking Law prohibits a bank in Switzerland from divulging information concerning its customers.³⁰ A violation of the bank secrecy law

securities on a foreign exchange would not be interpreted as a waiver of bank secrecy, even if it could be established that the transaction constituted fraud under foreign law:

The mere fact that person is a client of a [Swiss] bank is enough to evoke the [Swiss] bank secrecy law. It does not matter whether the relevant conduct was legal or illegal. In particular, it does not matter whether the client has violated the law of a foreign state when he claims the services of a Swiss banker.

SCHULTZ, *BANK SECRECY AND THE SWISS-AMERICAN TREATY ON LEGAL ASSISTANCE IN CRIMINAL MATTERS* 8 (1976) (passage translated by B. L. Nelson) [hereinafter cited as Schultz].

Moreover, the examples of "tacit consent" given by Professor Schultz directly after the phrase quoted by the SEC in the Release, *supra* note 1, at 32, indicate that the concept of "tacit consent" under Swiss law may not permit the result sought by the SEC:

Thus, the holder of an account impliedly releases a bank from its duty to keep secret that the holder has an account at the bank by instructing the bank to pay an amount to someone else from that account. If the client names his bank on his personal stationery, then he announces that he places no value on the secrecy of that banking relationship as concerns those persons to whom he writes with that stationery; yet he does not in any way permit the bank to let everyone know of this relationship or to give out information concerning the transactions of his account.

Schultz, *supra*, at 11 (passage translated by Mr. Nelson).

29. A fair interpretation of other sections of the text on Swiss bank secrecy laws quoted in the Release indicates that Swiss banks would violate secrecy laws by cooperating with the SEC in its requests for evidence:

It is understood that the [Swiss] bank may, on its own initiation, send to a customer the information which the customer needs in order to provide the information requested from him by certain public officials, especially tax officials. The customer is then free to provide or not to provide that information. It would, however, violate the [Swiss] bank secrecy law to issue such information directly to the public official concerned, unless a legal regulation would oblige or at least empower the bank to do so.

Schultz, *supra* note 28, at 11-12 (passage translated by B. L. Nelson).

From this quotation, it can again be surmised that placing an order with a Swiss bank to execute a transaction on a U.S. stock exchange may well not be interpreted under Swiss law as a waiver of the protection of the Swiss bank secrecy law.

30.

1. The Swiss law governing unauthorized disclosures of bank secrets is set forth below: Whoever divulges a secret entrusted to him in his capacity as officer, employee, mandatory, liquidator or commissioner of a bank, as a representative of the Banking Commission, officer or employee of a recognized auditing company, or who has become aware of such a secret in this capacity, and whoever tries to induce others to

can lead to imprisonment of up to six months or a fine of up to 50,000 Swiss francs.³¹

Swiss law recognizes exceptions to the protection of bank secrecy law. Such exceptions include express waivers by the customer, either oral or written,³² and implied waivers established by the conduct of the customer.³³ An example of waivers implied by the conduct of the customer is the naming of his bank on his personal stationery. This act establishes that the customer waives his right as to the existence of the banking relationship.³⁴ It does not establish a waiver concerning any transactions conducted by the bank.³⁵

Recognition of the waiver-by-conduct doctrine would go beyond the scope of waivers currently established under Swiss law. Accordingly, there is no basis in Swiss bank secrecy law to conclude that the doctrine of waiver-by-conduct would be recognized as an exception. In the absence of an international understanding, the scope of waivers currently recognized under Swiss law is strictly limited to the clear intent of the customer manifested either by express consent or by unambiguous conduct. It does not currently extend to presumptions established by foreign legislation.

Swiss banking law has already addressed the issue of requests for information from foreign authorities. In general, Swiss banks may relay the request to a customer, who handles it as he sees fit.³⁶ It would be a violation of Swiss bank secrecy law for the bank to respond directly to the request for information.³⁷ As regards requests for information from the SEC, a special arrangement has been worked out since 1982 which deviates from the general rule.

Recent developments in Switzerland indicate that securities fraud on U.S. markets originating abroad can be more effectively prosecuted through consultation and negotiation, rather than adoption of the waiver-by-conduct doctrine.³⁸ In 1982, the SEC negotiated agreements with the Swiss

violate professional secrecy, shall be punished by a prison term not to exceed six months or by a fine not exceeding 50,000 francs.

2. If the act has been committed by negligence, the penalty shall be a fine not exceeding 30,000 francs.
3. The violation of professional secrecy remains punishable even after termination of the official or employment relationship or the exercise of the profession.
4. Federal and cantonal regulations concerning the obligation to testify and to furnish information to a government authority shall remain reserved.

Bank Gesetz (Switz) art. 47, *reprinted in Crime and Secrecy: The Use of Offshore and Companies*, Staff Study of the Subcommittee on Investigations of the Senate Committee on Governmental Affairs, 98th Cong., 1st Sess. (Comm. Print Feb. 1983).

31. *Id.*

32. Schultz, *supra* note 28, at 32.

33. *Id.* at 8.

34. *Id.* at 11.

35. *Id.*

36. *Supra* note 29, at 11-12.

37. *Id.*

38. The course of consultations and negotiations between the U.S. government, including

Bankers' Association and with the Swiss Federal Department of Foreign Relations and achieved many of the objectives which the SEC hopes to achieve elsewhere through enactment of the waiver-by-conduct doctrine. Most recently, on May 1, 1985, the Swiss government published draft

the SEC, and Switzerland suggests an alternative approach to the effective protection of U.S. securities markets from fraud originating abroad. On July 14, 1982, the Swiss Bankers' Association (SBA) and the SEC entered into "Agreement XVI of the SBA with regard to the handling of requests for information from the SEC on the subject of misuse of inside information." *Reprinted in J. FEDDERS, J. HARRIS, R. OLSEN & B. RISTAU II TRANSNATIONAL LITIGATION: PRACTICAL APPROACHES TO CONFLICT AND ACCOMMODATIONS*, 1301-1316 (1984) [hereinafter referred to as *TRANSNATIONAL LITIGATION*]. In Agreement XVI, the SBA establishes a special commission of inquiry ("Commission") to handle requests for information concerning insider trading from the SEC (Articles 2 and 3). The Commission agrees to accept such inquiries as are transmitted to it through the Swiss Federal Office for Police Matters (Articles 1 and 3) and to forward them to the appropriate Swiss bank (Article 4(1)). The bank, in turn, contacts its customer and requests the customer to submit evidence and information in response to an inquiry (Article 4(2)). The bank files a report with the Commission, including the identity and address of the customer and information and evidence received from the customer concerning relevant transactions (Article 4(3)). The Commission agrees to submit a report to the Swiss Federal Office for Police Matters (to be forwarded to the SEC) unless the Commission is notified that the SEC has not requested information concerning this Swiss bank customer or that the customer is not an "insider," as defined in the Agreement (Article 5). Agreement XVI also contains a provision for blocking the customer's account to freeze illicit gains and remitting them to the SEC (Article 9).

In the wake of Agreement XVI, the SEC and the Swiss Federal Department of Foreign Affairs entered into a Memorandum of Understanding on August 31, 1982 (MOU), *reprinted in TRANSNATIONAL LITIGATION*, *supra* at 1287. The MOU establishes that an investigation conducted by the SEC falls within the Treaty between the United States and the Swiss Confederation on Mutual Assistance in Criminal Matters, *done* May 23, 1983, 27 U.S.T. 2019 (*entered into force* January 23, 1977) [hereinafter cited as *Mutual Assistance Treaty*], if such investigation "relates to conduct which might be dealt with by the criminal courts." (MOU, II.3(a)). *Id.* at 1291. The MOU also establishes that insider trading ("transactions effected by persons in possession of material non-public information") could be an offense under the Swiss Penal Code. (MOU, II.3(b)). *Id.* at 1291-92. The MOU concludes that "it will often be possible for compulsory measures to be ordered under the Treaty in order to assist the SEC in obtaining information from banks that executed the securities transactions in the United States that are the subject of the request for assistance" (MOU, II.3(b)). *Id.* at 1292.

Through these negotiations, the SEC has been able to gain acceptance in Switzerland for two of the principles which it hopes to impose by legislation elsewhere. First, the Swiss authorities have agreed that the principles set forth in an agreement between the SEC and the SBA shall govern the banking relationship between Swiss banks and their customers. (MOU, III(2)). *Id.* at 1294. ("This [Agreement XVI] will also govern the relationship between the signatory [Swiss] banks and the clients placing orders with the signatory banks for execution in the United States securities markets.") *Id.*

Second, the Swiss banks have implemented a form of waiver-by-conduct. Pursuant to Agreement XVI, Swiss banks have circulated a "Declaration of Agreement to . . . Agreement XVI of the Swiss Bankers' Association." *See, e.g., TRANSNATIONAL LITIGATION*, *supra* at 1317-18 for the form circulated by one Swiss concern to its customers. The Declaration gives customers the option of accepting or rejecting the terms of Agreement XVI. In the event that a customer rejects Agreement XVI, then the Declaration provides that "no further orders can be executed on his behalf on U.S. stock exchanges." It further provides: "In the case of the undersigned continuing to give the bank orders to be executed on U.S. stock exchanges after receipt of these documents, the remitting of such orders automatically constitutes his agreement to the stipulations of Agreement XVI of the Swiss Bankers' Association." *Id.* at 1318.

legislation making insider trading a criminal offense in Switzerland.³⁹ Adoption of this draft, which is considered a formality,⁴⁰ would bring insider trading within the scope of the Treaty for Cooperation in Criminal Matters between the United States and Switzerland.⁴¹ Once insider trading is within the scope of the Treaty, prosecution of fraud on U.S. securities markets originating in Switzerland should be greatly facilitated through the use of the Treaty.⁴²

B. GERMANY⁴³

Under German law, bank secrecy is guaranteed by the Basic Law of the German Federal Republic.⁴⁴ It is based upon both the customer's right to privacy and the Bank's right to freedom of conduct in its commercial activities. Under certain circumstances, the bank secrecy law permits the disclosure of credit information, e.g., if the customer has named the bank as a credit reference.⁴⁵ Germany also requires disclosures in derogation of bank proceedings in criminal trials⁴⁶ and in tax proceedings.⁴⁷

Under bank secrecy rules, unequivocal acts and consents short of written consents are recognized (e.g., naming the bank as a credit reference). However, the extent of the waivers recognized is narrowly construed and would not include waivers established by implication under foreign law. In addition, the German Data Protection Law generally prohibits the transmission of personal data unless a written and unequivocal permission of the client is obtained.⁴⁸ This law does not contain any provision regarding

The validity of this notice has yet to be tested under Swiss law. However, the important point is that the SBA adopted this approach as a result of consultation and negotiation with the SEC.

39. *The Economist*, May 4, 1985, at 82-83.

40. 17 SEC. REG. & L. REP. (BNA), 797 (May 3, 1985).

41. It is necessary that the acts giving rise to the request for cooperation constitute a criminal offense in both the United States and in Switzerland. Mutual Assistance Treaty, *supra* note 38.

42. Mutual Assistance Treaty, *supra* note 38, at art. 4.

43. The author acknowledges the contribution of Utz P. Toepke of Schwartz, Klink & Schreiber in the preparation of the materials on the Federal Republic of Germany.

44. See III CANARIS, GROSSKOMMENTAR HGB 3, n. 39 (3d. 1981), citing article 2 subparagraph 1 and article 12 of the German Basic Law (*Grundgesetz*).

45. Cf. Schraepfler, *Kreditauskunft—Einschränkungen des Bankgeheimnisses*, 1972 NEUE JURISTISCHE WOCHENSCHRIFT 1837.

46. StPO §§ 53, 161 a (Criminal Procedure Law).

47. Abgabeordnung §§ 90, 93. Information in derogation of the bank secrecy law must also be disclosed for certain statistical purposes: Law on the Banking System (Gesetz ueber das Kreditwesen—KWG) § 44; Law on External Trade (Aussen-Wirtschaftsgesetz—AWG) § 44; Law on Statistics for Federal Purposes (Gesetz ueber Statistik fuer Bundeszwecke—Stat Ges) § 110.

48. Gesetz zum Schutz von Missbranch personenbezogener Daten bei der Datenverarbeitung (Bundesdatenschutzgesetz—BDSG), dated January 27, 1977, effective January 1, 1978, in 1977, BGBI. I, p. 201.

implied permission of disclosure of personal data.⁴⁹ However, it has been interpreted to exclude any general assumption of a tacit consent to the transmission of personal data by the person whose data has been stored.

C. AUSTRIA⁵⁰

Under Austrian legislation, a bank is forbidden from disclosing any information concerning the banking relationship of its customers.⁵¹ Violation of these principles involves criminal sanctions.⁵² Austrian law does recognize exceptions to the protection of bank secrecy for disclosures in connection with criminal trials, fiscal and probate proceedings and customary credit information.⁵³ In all other cases, however, the Austrian law permits disclosure only "if the client explicitly and in writing agrees to disclosure."⁵⁴

As a general matter, Austrian law recognizes an implied consent,⁵⁵ but it requires that the implied consent be unambiguous so that there is no reason to doubt the customer's intention as evidenced by his actions.⁵⁶ For example, the action of the bank customer in placing a "buy" or "sell" order on a U.S. securities market—even in absence of the bank secrecy law—would not unambiguously indicate that he consents to the disclosure of information. Furthermore, the notice to be given in the standard contracts issued by U.S. broker-dealers to foreign banks giving notice of the waiver-by-conduct could not be used to constitute constructive notice to the banks' customers and to imply their consent. Such notice would be "contra bonos mores" and null and void under Austrian law.⁵⁷

D. UNITED KINGDOM⁵⁸

The law of the United Kingdom imposes on banks located there an implied obligation not to disclose information concerning customers, in-

49. See Thilo, *Bankgeheimnis, Bankauskunft und Datenschutzgesetz*, 1984 NEUE JURISTISCHE WOCHENSCHRIFT 582, at 584.

50. The author acknowledges the contribution of Dr. Hans Frieders of Frieders, Puschner & Tassul in the preparation of the materials on Austria.

51. Austrian Credit Act of January 24, 1979, § 23(1) Federal Law Gazette (Bundesgesetzblatt (BGBl) 1979 63, i.d.F BGBl 1982/370 [hereinafter referred to as Austrian Credit Act].

52. Austrian Credit Act § 34(1).

53. Austrian Credit Act § 23(2).

54. *Id.*

55. Austrian Civil Code § 863.

56. *Id.*

57. Austrian Civil Code § 879(3).

58. The author acknowledges the contribution of John K. McCall of Freshfields in the preparation of the materials on the United Kingdom.

cluding their identity, obtained in the course of the banking relationship.⁵⁹ Exceptions to this implied duty of confidentiality have been recognized where disclosure is compelled by the laws of the United Kingdom (e.g., banking, tax and company statutes)⁶⁰ and where the interests of the bank require disclosure (as in a suit by the bank against its customer).⁶¹

Exceptions also exist where the disclosure is made pursuant to the express or implied consent of the customer.⁶² The existence of such a consent is a question of fact.⁶³ It is unlikely that the waiver-by-conduct proposal would be held to create an implied consent under the laws of the United Kingdom since the practice of banks in the United Kingdom is to require written consents.

English courts have ordered banks to disclose customer information concerning fraud perpetrated by customers through the agency of U.K. banks.⁶⁴ However, such orders are exceptional.⁶⁵ Disclosure has been held to be in the public interest where there is more than a mere suspicion of fraud or criminal activity.

This exception was applied, for example, in favor of the SEC in the *Santa Fe* case.⁶⁶ In that case, the court ruled that there is "a public interest, and a very strong one, in not permitting the confidential relationship between a banker and client to be used as a cloak to conceal improper or fraudulent activities, evidence of which would otherwise be available to be used in legal proceedings, whether here or abroad."⁶⁷

As indicated, English courts will under certain circumstances order banks to disclose customer information. However, the factors relevant to a U.K. court in determining whether to order disclosure would not be enhanced by the waiver-by-conduct doctrine. On the contrary, such an attempt to influence the deliberations of the courts in the United Kingdom through an extraterritorial exercise of jurisdiction considered excessive by English stan-

59. *Tournier v. National Provincial and Union Bank of England* [1924] 1 KB 461; *XAG v. A Bank* [1983] 2 ALL ER 464.

60. Bankers' Book Evidence Act § 7 (1879); Taxes Management Act §§ 13, 17, 20, 24 (1970)(bank must disclose list of persons beneficially entitled to stocks registered in the name of the bank or its nominees, Income and Corporation Taxes Act § 481 (1970); Companies Act § 74 (1981)(investigation of a public company of interests in its shares).

61. In *Tournier*, 1 KB 461, the court *in dictum* envisioned an instance where a bank might be entitled to disclose otherwise confidential information about a customer in the course of litigation against that customer. In *XAG v. A Bank* [1983] 2 All ER 464, the court rejected the argument that a bank be allowed to disclose information about a customer to comply with a court order.

62. In *Tournier*, Atkin L. J. wrote: "the extent to which [the customer] authorizes information to be given on [a banker's reference] must be a question to be determined on the facts of each case." [1924] 1KB 461 at 486.

63. *Id.*

64. *Bankers Trust Co. v Shapiro* [1980] 2 All ER 353.

65. *XAG v. A Bank* [1983] 2 All ER 464. The bank concerned gave notice of appeal, but this appeal did not proceed.

66. *SEC v. Certain Unknown Purchasers . . . (the Santa Fe case)*, 81 Civil 6553 (S.D.N.Y. 1981). See SEC Release Nos. 9484 and 9485 (Oct. 26, 1981).

67. *Id.*

dards would be "distasteful" to a U.K. court and could have the opposite effect.⁶⁸

E. FRANCE⁶⁹

The French Criminal Code provides that professionals shall not disclose secrets entrusted to them by virtue of their relationship with a customer or client.⁷⁰ Recent French legislation has extended the obligation of professional secrecy to banks located in France.⁷¹ The sanction for a violation of

68. The attempts of the United States courts to compel discovery in the United Kingdom have led to the adoption of one of the best-known "blocking statutes," the Protection of Trading Interests Act 1980 [hereinafter the Act]. The Act enables the Secretary of State of the United Kingdom to prevent compliance with a request to produce evidence in several instances, including the following: where the order to produce evidence infringes on the jurisdiction of the United Kingdom (Section 2(2)(a)), where the order is prejudicial to the sovereignty of the United Kingdom (Section 2(2)(a)), or where the order to produce evidence is not made for the conduct of on-going civil or criminal proceedings (Section 2(3)(a)).

Courts in the United Kingdom have expressed their aversion to the extraterritorial application of U.S. Laws in several other contexts. In *British Nylon Spinners Ltd. v. Imperial Chemical Industries Ltd.* [1952] 2 All ER 780, a case involving a contract between English nationals, the court confirmed an interlocutory injunction, thereby preventing ICI from complying with an order of a U.S. District Court to produce evidence. In that case, Denning L. J. wrote, "The writ of the United States does not run in this country, and, if due regard is had to the comity of nations, it will not seek to run here." See also *Rio Tinto Zinc Corporation, et al. v. Westinghouse Electric Corporation* [1978] 1 All ER 434. (Requests for evidence from companies in the United Kingdom outside the legislative jurisdiction of the United States for the purpose of investigating alleged breaches of U.S. antitrust law constitute an infringement of U.K. sovereignty), and *Radio Corporation of America v. Rowland Corporation* [1956] 1 All ER 549. But see *British Airways Board v. Laker Airways Ltd., et al.* [1984] 3 All ER 39 (British Airways voluntarily subjected itself to the legislative jurisdiction of the United States, including the reach of its antitrust legislation, by obtaining licenses from the United States Civil Aviation Authority and operating scheduled services between the United States and the United Kingdom.).

69. The author acknowledges the contribution of Pierre Descheemaeker of Baudel, Sales, Vincent & Georges in the preparation of the materials on France.

70. Physicians, surgeons, . . . and any other individual who holds, by reason of his or her position or employment, or through a temporary or permanent assignment, secrets entrusted to him or her, and who—except in those cases where the law requires them to act as an informer—shall have revealed those secrets, shall be punished by a jail sentence of from one to six months and by a fine of from FF 500 to FF 8000.

French Criminal Code art. 378.

71. Any member of a Board of Directors or, as the case may be, of a Supervisory Board and any individual who, for any reason whatsoever, participates in the management and operations of a credit institution or who is employed by it, shall be subject to professional secrecy under the terms and sanctions set forth by Article 378 of the French Criminal Code.

In addition to those cases where a statute so provides, professional secrecy cannot be opposed to the Banking Commission or to the Bank of France, or to judicial authorities acting within the scope of criminal proceedings. Article 57.

Law No. 84-46 of January 24, 1984 "On the Operation and Supervision of Credit Institutions" art. 57 (1984 J.O. at 390).

professional secrecy is imprisonment of up to six months and a fine of up to 8000 French Francs.⁷²

Exceptions to the obligation of professional secrecy are recognized only in the case of clear statutory authority and for written authorization provided by the customer.⁷³ The French Penal Code does not contain any provision for the recognition of a waiver-by-conduct. Authorization must be specific and supported by written documentation. In the case of banks, a clear statutory exception exists only for the disclosure of outstanding loans to the central bank authorities.⁷⁴

Since the applicable French law contains no provision for waiver-by-conduct, the doctrine advanced by the SEC would not be recognized by French banks. This result is supported by French public policy, as articulated in other legislation. France has adopted criminal sanctions against the disclosure of confidential information to foreign authorities.⁷⁵

F. LUXEMBOURG⁷⁶

Under Luxembourg law, Luxembourg financial institutions are obliged to keep secret the identity and business operations of clients. Violation of this law carries criminal sanctions. The protection of the Luxembourg bank secrecy law, however, may be waived by the client or by the bank if it is in the legitimate interest of the bank to do so. Since the secrecy exists for the benefit of the customer, the instances under upon which a bank may disclose information without the consent of the customer are strictly limited. It is therefore doubtful that the waiver-by-conduct doctrine would be recognized under Luxembourg law because there would be no evidence showing that the client was on notice of the existence of any such waiver or that he had given his consent to such a disclosure.

72. Article 378 of the French Criminal Code, *supra* note 70, at 55.

73. *Id.*

74. G. GAVALDA & J. STOUFFLET, *LE DROIT DE LA BANQUE*, 231-37, (1974). In addition, French banking practice also permits the disclosure among banks of confidential information necessary to conduct transactions. *Id.* at 404.

75. Law No. 68-678 of July 26, 1968 "Relating to the Communication of Economic, Commercial, Industrial, Financial or Technical Documents and Data to Foreign Individuals and Entities," as amended by Law No. 68-678. As amended, it is a felony to provide foreign authorities, such as the SEC, with business-related information "which may serve as evidence for foreign judicial and/or administrative proceedings or within the scope thereof." *Id.* at art. 1. Sanctions for violation of the Law 68-678, as amended, include jail of from two to six months and/or fines of from FF 10,000 to FF 120,000.

76. The author acknowledges the contribution of Yves Prussen of Elvinger & Hoss in the preparation of the materials on Luxembourg.

G. HOLLAND⁷⁷

Under the principles of Dutch private international law (i.e., choice of law), transactions carried out by a Dutch bank through a United States broker on a United States securities market would be governed by United States law. In other words, the Dutch bank submits itself to the regulation and authority of the SEC by acting as an intermediary for its customers. Accordingly, a Dutch bank cannot refuse to give the SEC the requested information by invoking a rule of banking secrecy.

At the same time, under principles of Dutch private international law, the relationship between a Dutch bank and its customer is governed by Dutch law.⁷⁸ There is no basis in Dutch law, either by statute or case law, for bank secrecy.⁷⁹ In general, the Standard Conditions of the Dutch Bankers Association govern banking relationships in Holland. These Conditions are also silent as to the issue of bank secrecy. In fact, it is generally accepted that if a bank is under a legal obligation to disclose information, it can do so without breach of its obligation to the customer. It is only under an implied and generally accepted obligation to do so discreetly.

As a consequence, the SEC can discover the identities of individuals who execute transactions on U.S. markets through the agency of Dutch banks. However, the SEC does not need, and the Dutch are not likely to recognize, the waiver-by-conduct doctrine.

H. ARGENTINA⁸⁰

Under the national legislation of Argentina, banks cannot disclose information about the transactions which they execute or the information which they receive from customers.⁸¹ The statute expressly provides for limited exceptions in the case of trials, central bank operations or proceedings.⁸²

The national legislation does not contain an exception based upon the consent of the customer, but it is generally accepted that such an exception exists. The effective consent of customers is limited to their express consent and may not be implied.⁸³ Under the national legislation of Argentina, the National Securities Commission of Argentina is not authorized to obtain

77. The author acknowledges the contribution of L. H. W. Van Sandick and F. Heyning in the preparation of the materials on Holland.

78. Van Sandick, *Banking Secrecy—Financial Privacy and Related Restrictions (The Netherlands)*, 7(vi) INT'L BUS. LAW. 259 (1979).

79. Algemene Voorwaarden van de Nederlandse Bankiers Vereniging, as deposited with the District Courts of Amsterdam and Rotterdam on March 15, 1971.

80. The author acknowledges the contribution of Pedro de Elizalde of Allende & Brea in the preparation of the materials on Argentina.

81. Law No. 21526 § 39.

82. *Id.*

83. Civil Code of Argentina, Art. 874.

information directly from banks.⁸⁴ Consequently, it must obtain a court order to gain access to bank information.

It is unlikely that the SEC waiver-by-conduct doctrine would be recognized by banks in Argentina. Indeed, as in some other countries, recognition may be prohibited as contrary to public policy.⁸⁵

VI. The ABA Recommendation

On August 12, 1981 the American Bar Association adopted a resolution concerning the extraterritorial application of U.S. laws.⁸⁶ The recommendation provides in essence that federal agencies should seek to enforce U.S. laws overseas only after prior consultation with the Department of State and, whenever appropriate, with the foreign government involved when an important potential conflict of law and policy is involved.

The ABA's recommendation clearly applies to the SEC's waiver-by-conduct proposal because it involves an important potential conflict between the interest of the United States in maintaining the integrity of its securities markets and the interest of foreign countries in maintaining the inviolability of their banking systems. Pursuant to this recommendation, the SEC should not seek evidence abroad in derogation of foreign bank secrecy laws without first consulting with the Department of State and, whenever appropriate, with the foreign governments themselves.

The recommendation is based upon recognition of the fact that the appropriate application of U.S. laws abroad cannot always be determined by strict application of legal principles. Indeed, the legal principles which govern the extraterritorial application of laws differ in important ways from country to country. The recommendation also recognizes that the extraterritorial application of U.S. laws can compromise United States' foreign policy goals, especially where the rules governing the application of laws differ on an important issue.

It should be noted that the ABA proposal is not a guarantee of success for achieving administrative objectives. Consultations with the State Department and foreign governments may reveal that the exercise of administrative jurisdiction overseas is impossible without the cooperation of local governments and that unilateral attempts to extend U.S. law abroad would cause a deterioration in diplomatic relations. Such consultations can, however, also be useful for identifying issues upon which progress is possible and for avoiding needless aggravation.

84. Law No. 17811.

85. Recognition of the waiver-by-conduct doctrine would put the SEC in a better position than the Argentine Securities Commission, for which no exception to the bank secrecy law has been recognized.

86. See *supra* note 2.

VII. Conclusion

The integrity of the U.S. securities markets is essential for the prosperity of the United States. The efforts of the SEC to protect the U.S. securities markets from abuse and dishonesty, including fraudulent transactions originating abroad, should deserve and enjoy the support of thoughtful lawyers both in the United States and abroad. Still, the experience drawn from previous attempts to enforce other U.S. laws overseas and the specific nature of foreign bank secrecy laws indicates that adoption of the waiver-by-conduct doctrine would not enable the SEC to achieve its goal of promoting the prosecution of securities fraud originating abroad.

As regards the proper scope of the SEC's enforcement jurisdiction, the relevant legal issue is not the justification under U.S. principles for the extraterritorial application of U.S. laws, but the principles of law generally accepted abroad which justify foreign governments in refusing to cooperate with U.S. officials. Since principles of jurisdiction generally accepted abroad are rather categorically opposed to the extraterritorial enforcement of national legislation, it is reasonable to expect that foreign governments will refuse to cooperate with the waiver-by-conduct doctrine if it is enacted by Congress.

The specific provisions of foreign bank secrecy laws and the differences among those laws in various countries further limit the probable success of the waiver-by-conduct proposal. A survey of some of the relevant foreign bank secrecy laws indicates that the waiver-by-conduct proposal would not be recognized, in general, as an exception to foreign bank secrecy laws.

The ABA has previously recommended to the President and Congress that the extraterritorial application of U.S. laws by independent federal agencies should be preceded by consultations with the Department of State and, if appropriate, with the foreign governments involved. This recommendation applies to the doctrine of waiver-by-conduct. According to the ABA recommendation, the SEC should seek to resolve the conflict between the U.S. interest in the integrity of security markets and the interest of foreign countries in the inviolability of their banking systems primarily through consultation and negotiation instead of through the unilateral enforcement of U.S. laws overseas. Given the SEC's recent successes in its negotiations with Switzerland, consultation and negotiation need not be viewed as discouraging alternatives to congressional action.